Supreme Court, U.S.
FILED
APR 1 1986
JOSEPH F. SPANIOL, JR.
CLERK

No. 85-1480

In The

Supreme Court of the United States

October Term, 1985

UNITED STATES OF AMERICA,

Petitioner,

v.

MERCHANTS NATIONAL BANK OF MOBILE,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

RESPONSE TO PETITION FOR WRIT OF CERTIORARI

Brock B. Gordon
Alan C. Christian
P.O. Box 1988
Mobile, Alabama 36633
(205) 432-7682

Of Counsel:
Johnstone, Adams, Howard, Bailey and Gordon

Attorneys for Respondent, Merchants National Bank of Mobile

COCKLE LAW BRIEF PRINTING CO., (800) 835-7427 Ext. 333

16 pp

QUESTION PRESENTED

Section 6303(a) provides that the government, upon choosing to assess taxes unpaid by an employer, must give notice to each person liable for the unpaid tax. The question presented is whether, as a prerequisite to the government's maintenance of a civil suit to collect a lender's § 3505 derivative liability for said assessed taxes and extension of the statute of limitations for collection thereof, the government must comply with the general notice requirements of § 6303(a) and give notice of the assessment to the lender.

TABLE OF CONTENTS

	Page
Response to Statement	1
Reasons for Denying the Petition	3
Conclusion	11

TABLE OF AUTHORITIES

Page

CASES:

Cohen v. Gross, 316 F.2d 521 (3rd Cir. 1963) 6

Rambo v. United States, 492 F.2d 1060 (6th Cir. 1974), *cert. denied* 423 U.S. 1091, 96 S.Ct. 886, 47 L.Ed.2d 103 (1976) 6

Sedima, S.P.R.L. v. Imrex Co., Inc., 473 U.S. —, 105 S.Ct. —, 87 L.Ed.2d 346 (1985) 7

United States v. American Bank & Trust Co., No. 85-1615 (3d Cir.) 4

United States v. Associates Commercial Corp., 721 F.2d 1094 (7th Cir. 1983) 3, 4

United States v. Dixieline Financial, Inc., 594 F.2d 1311 (9th Cir. 1979) 3, 4, 6

United States v. Harvis Construction Co., No. 86-1540 (9th Cir.) 4

United States v. Hunter Engineers & Constructors, Inc., No. 84-2652 (9th Cir. argued Nov. 20, 1985) 4

United States v. Jersey Shore State Bank, 781 F.2d 974 (3d Cir., 1986) 4, 5, 7

United States v. Messina Builders & Contractors Co., No. 85-2505 (8th Cir.) 4

United States v. United California Bank, No. 85-1873 (9th Cir.) 4

United States v. Walker, 217 F. Supp. 888, 890 (W.D.S.C. 1963) 6

STATUTES:

Internal Revenue Code of 1954 (26 U.S.C.):

§ 3505 ..... 2, 3, 4, 5, 7, 8, 9

§ 3505(a) 2, 6, 8

TABLE OF AUTHORITIES—Continued

	Page
§ 3505(b)	2, 6, 8
§ 6011(a)	10
§ 6204	10
§ 6303(a)	*passim*
§ 6501	8
§ 6502	2, 8, 11
§ 6672	8
§ 6901	8
§ 7401	2

MISCELLANEOUS:

U.S. Const., Fifth Amendment	11

No. 85-1480

In The

Supreme Court of the United States

October Term, 1985

UNITED STATES OF AMERICA,

Petitioner,

v.

MERCHANTS NATIONAL BANK OF MOBILE,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

RESPONSE TO PETITION FOR WRIT OF CERTIORARI

RESPONSE TO STATEMENT

1. On November 9, 1977, the Commissioner made an assessment of employment taxes unpaid by Dri-Mix Products, Inc. (hereinafter "Dri-Mix") for the third quarter of 1977 and a similar assessment for employment taxes unpaid by Dri-Mix on May 15, 1978 for the fourth quarter

of 1977. The government never gave the Merchants National Bank of Mobile (hereinafter "MNB")[1] notice under § 6303(a) of the Internal Revenue Code[2] of said assessments.

Section 6303(a) provides the general statutory notice rule for collection actions under Subtitle F, including § 7401, which authorizes the Secretary of the Treasury to initiate civil proceedings for § 3505 tax collection, such as the case herein. The statute provides that "[w]here it is not otherwise provided by this title, the Secretary or his delegate *shall* . . . within sixty (60) days, after the making of an assessment of a tax pursuant to section 6203, give notice to each person liable for the unpaid tax . . .". (Emphasis added). The government did not give § 6303(a) notice to MNB, and § 3505 does not "otherwise provide" that notice was not required. Dri-Mix failed to pay the taxes assessed.

2. On March 18, 1983, some five and one-half (5½) years after assessment of the taxes unpaid by Dri-Mix without notice to MNB, the government brought this action in the United States District Court for the Southern District of Alabama against MNB, for so-called lenders' liability under §§ 3505(a) and (b), asserting the right to do so under the post-assessment extended statute of limitations of § 6502.

---

[1]Subsequent to the filing of the complaint in this matter, MNB was merged into, and is now known as, First Alabama Bank.

[2]Unless otherwise noted, all statutory references are to the Internal Revenue Code of 1954 (26 U.S.C.), as amended.

MNB answered said complaint and, after discovery, moved for summary judgment on the basis that the government's failure to give § 6303(a) notice to MNB precluded the government's civil action to impose § 3505 liability for the unpaid taxes. The District Court, relying on *United States v. Associates Commercial Corp.*, 721 F.2d 1094 (7th Cir. 1983), granted MNB's motion for summary judgment.

3. Petitioner appealed to the Eleventh Circuit Court of Appeals, and that Court, relying on *Associates*, affirmed the grant of summary judgment in favor of MNB. The Eleventh Circuit concluded that the government's "failure to provide MNB with the Section 6303(a) notice bars the present suit against MNB." 772 F.2d at 1524.

REASONS FOR DENYING THE PETITION

At the time of its opinion on October 7, 1985, the Eleventh Circuit decided an important question of federal tax law in a manner which squarely *agreed* with the only other appellate decision on the issue, the Seventh Circuit's opinion in *Associates*. Before *Associates*, the Ninth Circuit had addressed the interplay between §6303(a) and § 3505 in *United States v. Dixieline Financial, Inc.*, 594 F.2d 1311 (9th Cir. 1979), stating:

> 26 U.S.C. § 6303 requires that notice of the assessment be given within 60 days "to each person liable for the unpaid tax." If Dixieline was not given notice of the assessment against the employer of the tax for which it is being held liable, then the case may present a question as to the consequences that flow from that fact.

794 F.2d at 1313. The Seventh Circuit in *Associates* looked directly to, and answered the question left open in *Dixieline*, holding that one of "the consequences" is a bar to a subsequent suit to impose § 3505 liability for those taxes. The decision of the Eleventh Circuit adopted the *Associates* rule.

The government then obtained a ninety (90) day extension within which to file its petition for a writ of certiorari on the ground that it was awaiting a hopeful conflict in the circuits. After the time originally allotted for seeking a writ of certiorari, but within the extended period, the hoped for conflict appeared in *United States v. Jersey Shore State Bank*, 781 F.2d 974 (3d Cir. 1986).

MNB contends that because there was no conflict in the circuits at the time of or created by the opinion below, it is entitled to the finality of the judgment in its favor and for which no basis for certiorari was timely asserted. If the government intends to pursue this matter which it now contends for the first time is of "considerable administrative importance," (Petition, p.5), it should be required to do so in response to a petition in *Jersey Shore*, or as appropriate in other pending cases.[3]

Furthermore, MNB contends that the issue sought to be reviewed herein by the government is so clearly in-

---

[3]Appeals on this issue are also currently pending in the Third, Eighth and Ninth Circuits in *United States v. American Bank & Trust Co.*, No. 85-1615 (3d Cir.); *United States v. Messina Builders & Contractors Co.*, No. 85-2505 (8th Cir.); *United States v. Harvis Construction Co.*, No. 86-1540 (9th Cir.); *United States v. United California Bank*, No. 85-1873 (9th Cir.); and *United States v. Hunter Engineers & Constructors, Inc.*, No. 84-2652 (9th Cir. argued Nov. 20, 1985).

appropriate for judicial determination that this Court should summarily deny the petition and leave the matter with Congress. The government's basic thesis is that "the practical effect of the decision below would be to nullify . . . an important part of the tax collection scheme." (Petition, p. 5). Whether the unambiguous general notice rule of § 6303(a), provided by Congress prior to adoption of § 3505, places an intolerable administrative burden on the government or not, Congress is the forum from which relief through statutory revision of the real or imagined burden should be addressed. Review by this Court is therefore inappropriate.

1. As revealed by the clear and well reasoned dissent of Judge Weis, the majority in *Jersey Shore* ignored the clear and unambiguous language of § 6303(a) and improperly concerned itself with the context of enforcement procedures under Subtitle F to reach its conclusion. The majority began with an examination of the statute itself, stating that the court would look beyond the express language of § 6303(a) to give force to presumed Congressional intent in only two circumstances: "where the statutory language is ambiguous; and where a literal interpretation would thwart the purpose of the overall statutory scheme or lead to an absurd result." *Id.* at 977.

The majority in *Jersey Shore* engaged in a painful convoluted analysis of § 6303(a) to then declare it "less than wholly unambiguous", *id.* at 978, focusing primarily not on the notice aspects of § 6303(a), but on the demand (for payment) aspects of the statute.

This focus on the demand aspects of § 6303(a) recognized the obvious: that the employer may have a different

numerical tax liability then the lender under §§ 3505(a) and (b). By such an analysis, the Third Circuit could find the statute "less than wholly unambiguous" only in the context of the government's internal administrative tax collection procedures, and not from the language of the statute itself. *Id.* at 978. However, the procedure by which the government conducts its tax collection activities cannot be allowed to rewrite the tax laws; the tax laws must control the procedures of the government.

The phrase "each person liable for the unpaid tax" is not "less than wholly unambiguous" unless "person" could mean only the "taxpayer". Congress obviously meant to include others, and the use of "person" undeniably confirms Congress' intent that, as a general rule, the minimum procedural safeguard under Subtitle F for collection of any tax liabilities, whether by administrative means or civil proceedings, must be notice of potential liability to all persons liable, whether direct or derivative, after assessment.[4] As Judge Weis pointed out, the "net effect of the Code revision urged by [the government] is to give less procedural protection to one secondarily

---

[4]As was stated in *Dixieline*, "[a]ssessment of tax as defined consists of no more than the ascertainment of the amount due and the formal entry of that amount on the books of the secretary. *See Rambo v. United States*, 492 F.2d 1060 (6th Cir. 1974), *cert. denied* 423 U.S. 1091, 96 S.Ct. 886, 47 L.Ed.2d 103 (1976); *Cohen v. Gross*, 316 F.2d 521 (3rd Cir. 1963). As was stated by the court in *United States v. Walker*, 217 F. Supp. 888, 890 (W.D.S.C. 1963); 'The Commissioner is required to assess the tax . . . rather than assess the taxpayer.'" 594 F.2d at 1312 (footnote omitted). The government, in having chosen to assess the tax and asserting that MNB is liable for the assessed tax, cannot escape the conclusion that MNB should receive § 6303(a) notice.

liable than to the primary obligor" who actually knows that the taxes have not been paid, producing an "anamalous result."[5] *Id.* at 984.

2. Petitioner's and the Third Circuit majority's focus on the Legislative History of §6303(a) is misplaced, simply because it provides no enlightment to their conclusions. Because § 6303(a) applies after assessment of the tax "unless otherwise provided", the majority should have focused on the Legislative History of §3505 to determine if Congress had "otherwise provided" therein. A review of such Legislative History shows that Congress was silent on the issue of exemption from § 6303(a) notice when enacting § 3505. As Judge Weis noted, "Congressional silence, no matter how clanging, cannot override the words of the statute." *Id.* at 984, citing *Sedima, S.P.R.L. v. Imrex Co., Inc.*, 473 U.S. —, 105 S.Ct. —, 87 L.Ed.2d 346, 358 n. 13 (1985).

The interrelationship of §6303(a) and § 3505 is highly significant. Without assessment, the statute of limitations against a lender for § 3505 liability is three (3)

---

[5]With notice, the employer is specifically apprised of the assessment, the nonpayment of taxes and the extension of the statute of limitations. The lender, on the other hand, would have no notice of the nonpayment of taxes, the extension of the statute of limitations, the need to preserve records, preserve testimony, prepare memoranda of events and circumstances concerning the loans, maintain contacts with lending officers or otherwise prepare a defense to said potential liability, nor would it have an opportunity to assure that its own liability were not exposed. Although the government recognizes that "notice and demand under section 6303(a) are chiefly designed to protect the taxpayer from surprise collection activity", (Petition, p.8), it does not explain its justification for taxation by ambush after five and one-half (5½) years herein.

years under § 6501. Upon assessment, the statute of limitations against a lender for § 3505 liability is extended for six (6) years under § 6502.

Congress acknowledged this distinction and clearly recognized the need for notice under § 6303(a) by not "otherwise providing" for notice under § 3505. As Judge Weis indicated, "[t]he likelihood of prejudice because of the loss or destruction of records by one secondarily liable is real and substantial." *Id.* at 984.

To this simple and logical statutory construction, the Third Circuit majority simply states that service of the summons and complaint is sufficient notice to the lender because the lender must have *made* direct payments in violation of §3505(a) or made loans with *knowledge* that the taxes would not be paid, establishing liability under § 3505(b). *Id.* at 980.

This response appears to rest on a presumption of guilt: the lender violated the law, knew or had notice of his violation of the law, and thus, needs no notice from the government even though the lender is called upon to defend itself from such allegations years after the transactions in issue. Moreover, this rationale fails to recognize practical commercial transactions, as the lender has merely loaned money to its customer.[6]

---

[6]This theory of "presumed guilt" is in diametric opposition to the concept of fundamental fairness and notice from the government to a person liable for unpaid taxes. Congress specifically rejected this theory of "presumed guilt" by not granting the government the power of separate notice and assessment for § 3505 liability, as in the case of penalties under § 6672 for certain responsible officers and § 6901 for certain transferees.

Petitioner's reliance on the Third Circuit's reasoning that the government's failure to assess taxes or to give notice thereof does not preclude it from exercising its common law right to sue a lender for the taxes is similarly misplaced.

As the Eleventh Circuit declared, § 3505 does not codify a common law liability, rather, it creates a secondary liability enforceable by the statutory procedure, stating:

> The United States also argues that even if § 6303(a) requires notice to third-party such as MNB, the failure to give notice does not preclude suit to collect on MNB's alleged § 3505 liability. The United States contends that it has an inherent common law right to sue to collect debts which is entirely independent of the assessment process. Appellant, however, ignores the fact that third-party derivative liability of the sort set forth in § 3505 is a creature of statutory, not comman law. This argument is therefore untenable.

772 F.2d at 1524, n. 1.

3. The most compelling part of the government's argument adopted by the Third Circuit majority is indeed the one most clearly reserved for Congress and not for this Court. The government argues that the requirement of §6303(a) notice would result in an unworkable enforcement scheme that would largely nullify an important part of the tax collection process. Such notice, the government continues, would impose a prohibitory investigative burden on the government.

Whatever merit this argument may have in a hypothetical case, MNB submits that it has no place before a judicial forum and clearly has no merit under the facts

in the present case. The government was investigating MNB as early as October 3, 1977, approximately ninety-six (96) days before notice of the assessment should have been given to MNB, (Supplemental Record, Deposition of Andreadas, p. 12, Exhibit 1), and actually prohibited MNB and Dri-Mix from paying the taxes in question from funds advanced by MNB once the government learned the taxes had not been paid. (Supplemental Record, Deposition of Tovar, pp. 36-58, 62, 73; Exhibits 14, 15; Deposition of Patrick, pp. 89-91).

The government argues, nevertheless, that the Commissioner "would find it virtually impossible to provide . . . notice of the sort that the court [has] ordered." (Petition, p. 13). Such a broad, unsupported statement clearly shows that the government fails to appreciate its own resources.[7]

Perhaps the most troubling aspect of the efforts of the government to have this Court, rather than Congress, rewrite § 6303(a) is that it results in taxation by ambush against lenders and other secondarily liable parties under

---

[7]For example, the government could commence an immediate investigation to determine if there are parties secondarily liable, assess the taxes, and then give appropriate § 6303(a) notice; reform the employer's withholding tax return pursuant to § 6011(a) such that lenders must be listed thereon and could be given a § 6303(a) notice as a matter of course; delay its assessment for any amount of time within three (3) years of the filing of the return, conduct an investigation, assess the taxes and then give the § 6303(a) notice; or perhaps make a supplemental assessment under § 6204, since the original assessment could be deemed incorrect "in any way" by failure of the employer to identify its lenders or the government to adhere to the § 6303(a) notice requirements to secondarily liable parties, and then give the required § 6303(a) notice.

the § 6502 extended statute of limitations. Such a unilateral and secret extension of the statute of limitations through failure to give notice to lenders of the underlying assessment against the employer may raise the serious Fifth Amendment due process concerns: the threat of taking of property without minimal due process. There is no basis to believe the government's assertion that the rule adopted by the Seventh and Eleventh Circuits constitutes an unworkable enforcement scheme, or will encourage lenders to return to net payroll financing, but there are fundamental rules of fair play and procedural due process recognized by Congress that mandate § 6303(a) notice to those lenders.

—o—

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

Brock B. Gordon
/s/ Alan C. Christian
P.O. Box 1988
Mobile, Alabama 36633
(205) 432-7682

Attorneys for Respondent, Merchants National Bank of Mobile

April 1986